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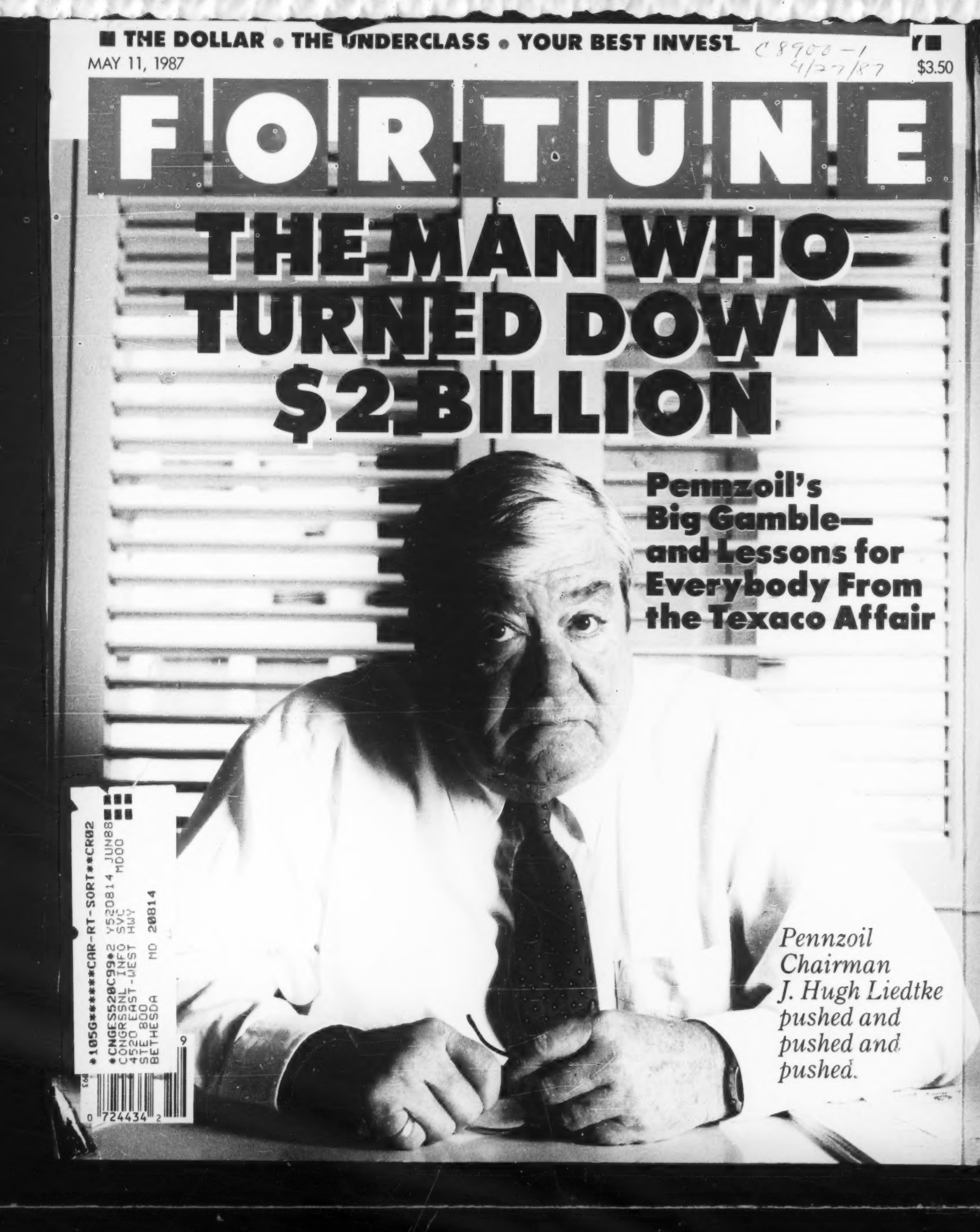
FORTUNE

THE MAN WHO TURNED DOWN $2 BILLION

Pennzoil's Big Gamble—and Lessons for Everybody From the Texaco Affair



Pennzoil Chairman J. Hugh Liedtke pushed and pushed and pushed.

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George Lange photographed the Pennzoil chairman at the Waldorf Towers in Manhattan. *See page 50.*

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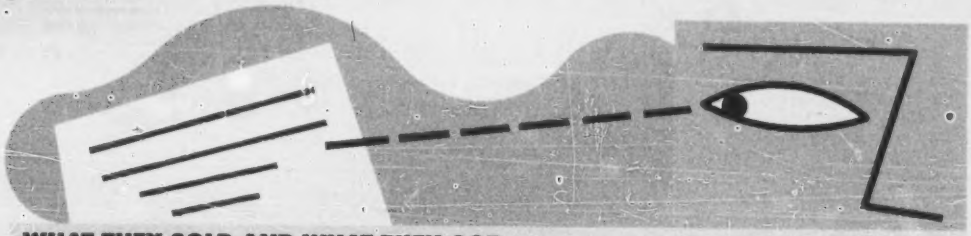


The declining wages of espionage

■ Think you can make a quick buck selling secrets to the Russians? Think again. Judging from those spies who have been caught, the espionage game pays rather poorly and the penalties can be stiff (see chart).

If the embassy security cases in Moscow and Leningrad are any indication, the spy profession has reached new lows. The principal remuneration the Marines allegedly got was what economists call imputed income, in this case sex with Soviet agents. Marine Sergeant Clayton John Lonetree reportedly received sex and just $3,500 for turning over names of U.S. undercover agents, among other data. However, formal charges against Lonetree do not say he received money for the information, and prosecutors are having trouble gathering evidence.

"The Soviets are notorious for being poor payers," says Phillip Knightley, a British spy sage who recently published *The Second Oldest Profession: Spies and Spying in the Twentieth Century.* He reckons that probably no U.S. document is worth millions to the Soviets. But an agent in the inner sanctum is another matter. Says Knightley: "A mole in the National Security Council could probably get $100,000 a month."

While the U.S. most likely follows much the same pay scale as the Soviets, at least it can lure a Russian spy with the prospect of a rich life in the West after the goods are delivered. The CIA reportedly has already paid former Russian diplomat Arkady Shevchenko more than $400,000 for spying for the U.S. from 1976 to 1978, when he defected. Since then Shevchenko made $150,000 writing a book, sold the book's film rights for $450,000, and gives lectures for up to $12,000 an appearance.

WHAT THEY SOLD AND WHAT THEY GOT

NAME	CLIENT	SERVICE RENDERED	FEE	STATUS
Sgt. Clayton John Lonetree	Soviet Union	Allegedly sold information about U.S. undercover agents in Moscow, 1985-1986	$3,500 and sex	Charged with espionage
Richard W. Miller	Soviet Union	Turned over FBI documents, 1984	Sex and a promise of $65,000	Serving a life sentence
Ronald Pelton	Soviet Union	Turned over information on U.S. intelligence gathering, 1980-1985	$35,000	Serving a life sentence
Jonathan Jay Pollard	Israel	Turned over classified documents including U.S. ship locations, 1984-1985	$45,000	Serving a life sentence
John A. Walker Jr. Arthur J. Walker Michael L. Walker Jerry A. Whitworth	Soviet Union	Turned over military documents including Navy cryptographic data, 1968-1985	$1 million	Serving jail terms from 25 years to 365 years

ANDRÉS VARNUCKEN

No need for want ads at the White House

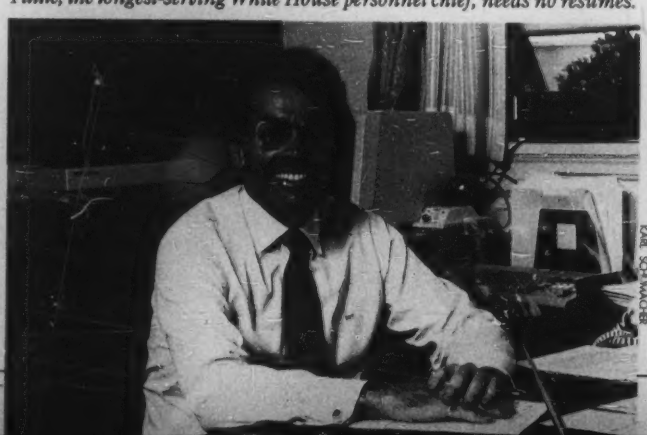
■ The post-Irangate departures of high-level officials such as Deputy Treasury Secretary Richard Darman and Navy Secretary John Lehman raise fears of a President bereft of his best and brightest. Not to worry. Says presidential personnel director Robert Tuttle: "People still want to serve this President."

Ironically, the Iran-contra scandal has helped White House recruitment efforts, though jobs often go begging at the end of a two-term presidency. With his Administration threatened, Ronald Reagan was able to attract a fresh team led by chief of staff Howard Baker. Outside the White House, the Administration has mostly filled high-level vacancies from within. Replacing Darman is M. Peter McPherson, a former administrator of the Agency for International Development. Taking CIA director William Casey's place is former FBI director William Webster. About a dozen candidates are vying for the FBI job.

Secretary of the Navy Lehman's successor is assistant secretary for reserve affairs James H. Webb, a Marine combat officer who has written best-selling books on Vietnam. Replacing assistant secretary for international security policy Richard Perle is fellow hard-liner Frank Gaffney Jr., a top Pentagon official.

Openings are hotly contested on independent commissions, where terms will extend beyond November 1988. Currently, a battle rages for the chairmanship of the Securities and Exchange Commission, vacated by John Shad, who has been nominated ambassador to the Netherlands. Among the contestants are Tuttle; Arthur Levitt Jr., chairman of the American Stock Exchange; U.S. District Court Judge Kevin Duffy; and Edward Fleischman and Charles Cox, both Republican members of the commission.

Tuttle, the longest-serving White House personnel chief, needs no résumés.



EARL DOTTER JR.

Getting ready for Mike Wallace

■ Is there anything Americans can teach the Japanese? Yes. How to deal with the probing, irreverent U.S. media. Japanese

TRADE

PROTECTIONISM CAN'T PROTECT JOBS

At least not without doing much more harm than good. In any case it is not needed. Despite the flood of imports, the U.S. is producing plenty of high-paying new jobs. ■ *by Michael McFadden*

IT IS axiomatic among protectionists that imports are wiping out the best red-blooded, high-paying U.S. manufacturing jobs and leaving the displaced workers to scrounge for a living as hamburger flippers. The protectionists make their case with a mixture of haunting portraiture—idled auto plants, shuttered steel mills, distraught ex-workers—and carefully selected statistics. The only answer, they say, is to get tough with our trading partners.

But is it? While imports have shot up some 50% since 1981, the U.S. has generated 7.6 million new jobs. Far more of them have been high paying than low paying (see table). Meantime, protectionist measures designed to help such industries as textiles, steel, and autos have not kept employment in them from shrinking drastically.

The protectionist point of view enjoys the support of powerful constituencies, including labor unions, whose ranks have thinned in recent years, manufacturers who would rather bleat than fight, and Democrats looking for campaign issues. Missouri Representative Richard Gephardt, a candidate for the 1988 presidential election, is sponsoring an amendment that would require the President to impose trade restrictions on countries that run sizable trade surpluses with the U.S. helped by unfair trade practices.

Powerful constituencies, however, cannot

REPORTER ASSOCIATE *Cynthia Hutton*

Quotas help preserve *the jobs of steelworkers like this Bethlehem employee, but only at an estimated annual cost of $750,000 per job.*

turn myth into fact. Yes, U.S. manufacturing employment has dropped some 9% from its 1979 peak. Visible pockets of pain remain as industry continues to restructure.

Some foreign manufacturers are getting special help from their governments—European steelmakers, for instance, are abetted by direct subsidies, import controls, and production quotas. Others enjoy markedly lower wage rates (though the strengthening yen has now lifted total compensation in Japanese manufacturing practically to U.S. levels). And until recently, the strong dollar penalized U.S. exports. But smokestack America's trade woes are due mainly to such old self-inflicted injuries as bloated payrolls, rigid union work rules, and indifferent management.

The protectionists got a big boost from a study published in December by the Joint Economic Committee. Produced by economists Barry Bluestone of the University of Massachusetts and Bennett Harrison of MIT, the JEC study contended that 58% of the eight million new jobs the U.S. economy created between 1979 and 1984 paid less than $7,000 a year, measured in 1984 dollars. It also made the dramatic assertion that the American middle class is shrinking.

The JEC study poured a few drops of new wine into an old bottle. A small group of economists have been advancing the argument of the disappearing middle class for several years, starting in the early 1980s when recession was playing havoc with employment and income growth. Every such claim has evaporated when put to rigorous examination, and the Bluestone-Harrison thesis is proving no exception.

FOR ONE THING, says Bruce Bartlett, a senior fellow at the Heritage Foundation, a conservative Washington research group, the study erroneously lumps full-time and part-time workers together to create the impression that job growth is occurring only in the low-paid categories. Of the 4.6 million jobs created between 1979 and 1984 that paid less than $7,000 a year, 1.7 million were part time. Excluding part-timers in all categories, Bartlett says, the proportion of low-paying jobs falls sharply, from 58% to 22% of the total. Does the surge of part-time work suggest an inadequacy in the U.S. job-creating mechanism? No, according to economists at the Bureau of Labor Statistics. Last year, for example, about 75% of part-time workers—many of them teenagers and retired people—were seeking part-time jobs.

Economists also fault the time periods used in the JEC study. Bluestone and Harrison compare job growth in 1979, a year when the economy had reached a cyclical peak, with job growth in 1984, when it was still recovering from the brutal 1981-82 recession. Bluestone and Harrison have since updated their figures; the 1985 data, they say, show that 44% of the new jobs since 1979 were in the low-wage category. Nonetheless, an examination of wage distribution among U.S. jobs over the past ten years shows that it is about the same as it was a decade ago.

The ten-year figures, moreover, mask a powerful shift in the kinds of jobs being created these days. Earnings classifications developed in the JEC study, updated in 1985 dollars, define low-paying jobs as those that

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THE PRICE OF PROTECTIONISM

INDUSTRY	TOTAL COSTS TO CONSUMERS 1984 in millions	NUMBER OF JOBS SAVED	COST PER JOB SAVED
Textiles and apparel	$27,000	640,000	$42,000
Carbon steel	$6,800	9,000	$750,000
Autos	$5,800	55,000	$105,000
Dairy products	$5,500	25,000	$220,000
Shipping	$3,000	11,000	$270,000
Meat	$1,800	11,000	$160,000

Quotas and other measures saved an estimated 751,000 jobs in these industries but are costing U.S. consumers $49.9 billion a year, according to economists Gary Hufbauer and Howard Rosen.

pay under $7,263, middle-pay jobs as $7,263 to $29,048, and high-pay as everything above. Using those classifications, high-paying new jobs increased 43% from 1981 to 1985 while low-paying jobs rose 25%; those in the middle increased 31%. As a result, high-paying jobs jumped from 14% of all jobs in 1981 to 16% in 1985. Low-end jobs fell from 33% to 31%, while the middle remained about the same. There is some evidence that the proportion of lower-paying jobs within each wage category has increased. But this trend appears partly due to baby-boomers taking jobs for the first time, and an increasing number of women entering the work force. Wages within each category should rise as the inexperienced workers advance.

Most of the new job growth has come in the service sector, which protectionists characterize as a sinkhole of dead-end jobs. Among the fields of growth: health care, law, and computer services. Pay levels seem likely to keep rising in services. Labor Secretary William Brock warns that the U.S. is heading for a critical shortage of skilled mechanics, teachers, nurses, and paralegals in years to come. At the same time, manufacturing is starting to generate a trickle of new jobs. Latest BLS data show that manufacturing employment rebounded to a seasonally adjusted 19.2 million at the end of last year, up 6.7% from its low of 18 million in December 1982. It is unlikely that the number will soon approach the June 1979 peak of 21.2 million,

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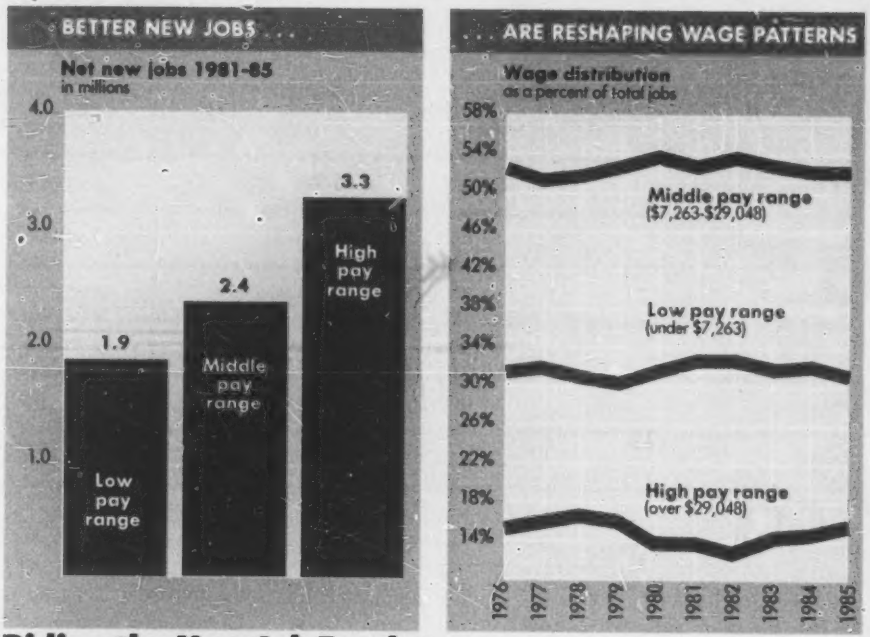


Riding the New Job Escalator

The high-paying new jobs the U.S. has created in recent years, virtually all in service industries, are pushing the wage distribution for all jobs higher. Low-range jobs are falling as a percent of the total.

but this does not mean that the U.S. industrial base is crumbling. Manufactured products continue to account for a solid 20% of GNP—just as they have for the past four decades—and rising output in the years to come will continue to add jobs.

Unquestionably, some or many of the workers who left manufacturing jobs for service jobs took pay cuts, though often they were victims of their unions' success in winning pay scales far out of line with productivity increases. Manufacturing wages averaged $396.01 a week in 1986, vs. an average service wage of $265.20. But in part the difference reflects the wage structures of mature manufacturing industries vs. younger service industries, as well as the relative youth of many service workers.

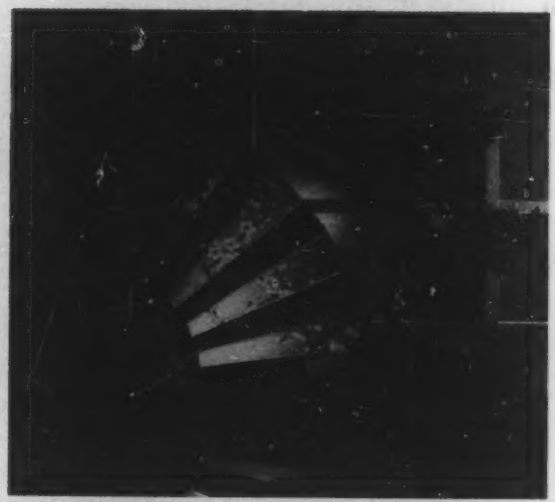
Wages alone aren't enough to tell if Americans are prospering. Richard McKenzie, an economist at Clemson University and a specialist in industrial labor policy issues, says personal income is a better measure, since it includes supplemental income such as pension payments, worker's compensation, and Social Security. Today such income equals 20.5% of an average worker's wages, up from 14.7% in 1973. The rise has helped boost personal income, measured in 1986 dollars, 12% since 1973 to $14,500.

In short, the numbers make it clear that the U.S. job-creating machine needs no protective tinkering. Other evidence suggests that protectionist measures adopted to date have not only saved far fewer jobs than they were supposed to but have also imposed economic costs so high that the measures may well destroy more jobs in the long run than they have saved.

Trade protection first hits the consumer's pocketbook. According to Gary Hufbauer, a professor of finance at Georgetown University and an international trade expert, quotas and tariffs cost U.S. consumers a walloping $66 billion in 1986. Hufbauer and Howard Rosen, a research associate at the Institute for International Economics in Washington, also calculate that American consumers are subsidizing jobs in industries like auto, steel, and textiles at costs ranging from $50,000 to $150,000 per job saved. Consumers spend $27 billion on textile and apparel subsidies alone. That works out to $42,000 per job in an industry with an average wage of $12,000. U.S. taxpayers would come out ahead by granting most of the workers whose jobs they are saving early retirement at full pay. These costs also add to the burdens of manufacturers hoping to compete with low-priced imports—expensive steel, for example, drives up the cost of building cars in Detroit.

It is difficult to credit protectionism with saving many jobs in any case. The so-called voluntary restraint agreements limiting the

SUPERIOR SERVICE UNFOLDS IN JAPAN.



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number of Japanese cars sold in the U.S. were meant to give Detroit time to become competitive with the Japanese. But in order to compete, U.S. carmakers have shed over 130,000 jobs since 1978, and the process is still not complete.

PROTECTIONISTS argue that the quotas reduced the pain of readjustment by letting automakers earn enough profits to preserve some jobs and help displaced workers find new ones. But quotas can be addictive, allowing industries to put off hard choices they must make to become fully competitive. Despite the soaring yen, which has driven up the prices of Japanese autos in the U.S. by some 10% so far, Detroit still insists it needs protection. In January, Japan agreed to extend restraints for a seventh year.

A long history of protection has not kept the textile industry from losing jobs either. In the decade after the U.S. signed a multilateral restraint agreement in 1962, employment in the textile and apparel industry rose 9%. But the aggregate figures hid massive job losses in the Northeast as textile manufacturers reduced labor costs by moving south and west. Between 1960 and 1970, textile employment in New England declined 34%, while increasing 19% in the South. Then between 1973 and 1984, as the industry increasingly automated, total employment fell 28% to 722,000—20% below its 1961 level.

If Congress does pass protectionist legislation, the U.S. should expect its trading partners to pay it back in kind. Using 1984 data, Lester Davis, an economist specializing in international trade at the Commerce Department, estimates that every $1 billion of exports the U.S. generates supports 25,800 jobs. Overall, he calculates, 5.5 million Americans hold jobs that are linked to exports.

How many of those jobs would go in a trade war? It's hard to say, but it is instructive to remember that the infamous Smoot-Hawley Act, which effectively closed U.S. markets to imports, helped bring on the Great Depression. As the world economy slumped and America's trading partners retaliated, U.S. exports shrank from 6% of GNP in 1930 to 4.3% in 1933. An estimated one million workers in export-related industries lost their jobs. The price of severe protection today could be a world recession and possibly another depression. Either would cost more jobs than the protectionists can ever dream of saving. F

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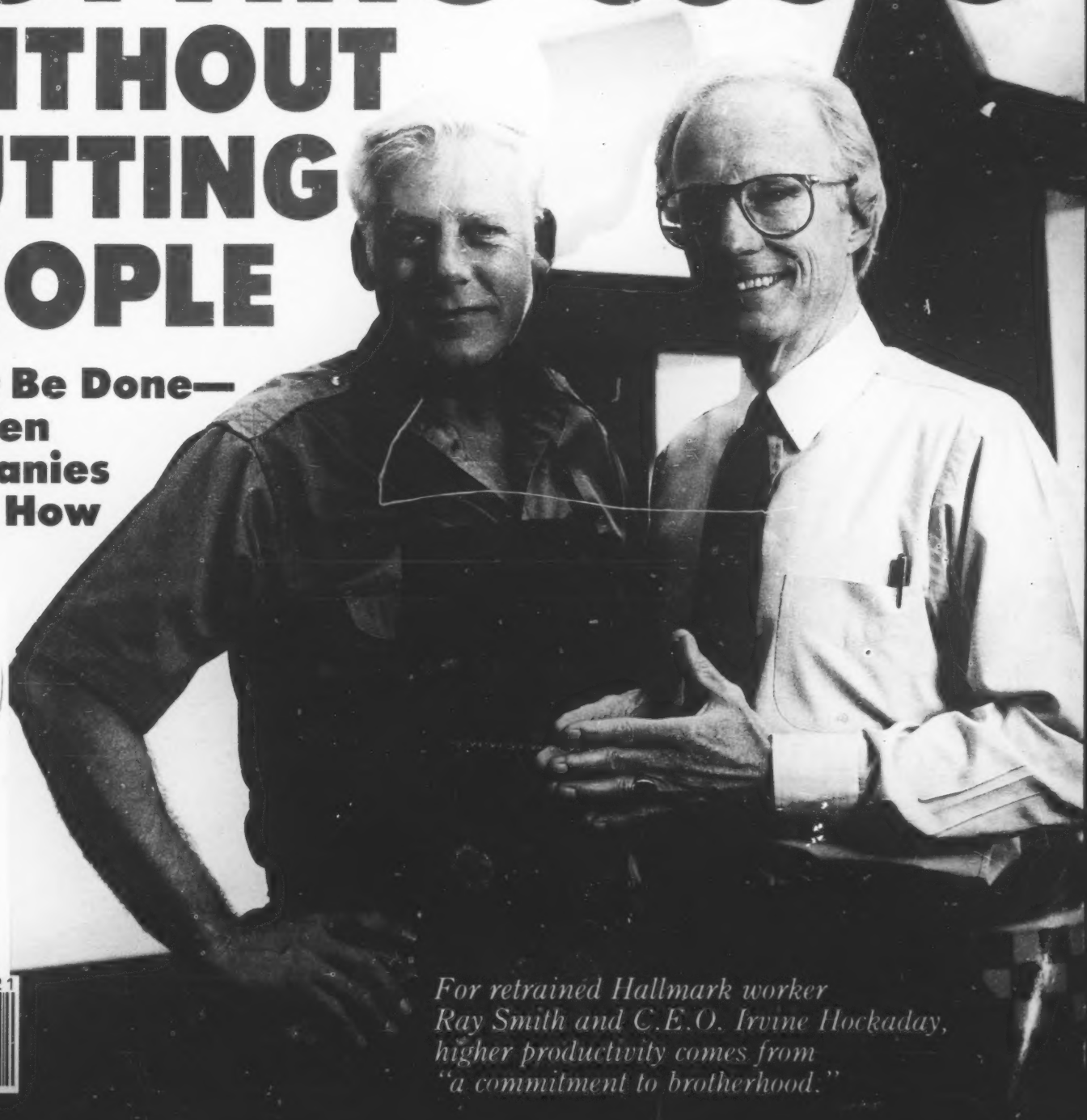
FORTUNE

CUTTING COSTS WITHOUT CUTTING PEOPLE

It *Can* Be Done—And Ten Companies Show How



For retrained Hallmark worker Ray Smith and C.E.O. Irvine Hockaday, higher productivity comes from "a commitment to brotherhood."

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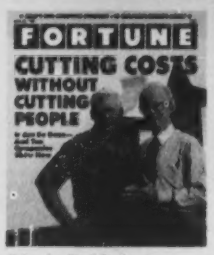

Maria Robledo photographed Hallmark worker Ray Smith and C.E.O. Irvine Hockaday in front of a sculpture at the company's Kansas City headquarters. *See page 26.*

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LETTERS

Corrections

FORTUNE's *Directory of the 500 Largest U.S. Industrial Corporations (April 27) should have listed the 1986 total return to stockholders and the ten-year average return to stockholders for the following companies as: Colt Industries, 42.40% (rank: 84); 23.04% (rank: 88). Digital Equipment, 58.11% (rank: 37); 14.55% (rank: 229). FMC, 102.83% (rank: 7); 23.62% (rank: 82). Fuqua Industries, 23.76% (rank: 181); 27.28% (rank: 47). Owens-Corning Fiberglas, 151.96% (rank: 3); 14.93% (rank: 223). Russell Corp., 83.53% (rank: 16); 40% (rank: 5). Johnson Controls, 21.07% (rank: 200); 20.76% (rank: 122). For Figgie Corp., 1986 earnings per share should have been 25.4% and ten-year earnings-per-share growth rate 13.68% (rank: 86). Amdahl Corp.'s 1986 sales were $966,349,000 (rank: 310). Net income for Baxter Travenol Laboratories was $444,000,000 (rank: 39). Harcourt Brace Jovanovich's net income was $70,476,000 (rank: 194). The headquarters of American Brands is in Old Greenwich, Connecticut. CF Industries, a farm cooperative, has no stock market value. Procter & Gamble's industry code should have been 43, soap and cosmetics.*

In "The New Show at Neiman-Marcus" (April 27), FORTUNE *referred to the president and chief operating officer of General Cinema as Richard Tarr. His name is Robert J. Tarr Jr.*

In "The Great Leap of Computer Graphics" (News/Trends, April 27), FORTUNE *described the image on the screen as a fractured pelvis. The Johns Hopkins doctors are in fact looking at a patient's shoulders and ribs.* ■

Address letters to FORTUNE, Time & Life Building, Rockefeller Center, New York, N.Y. 10020. Letters may be edited for purposes of clarity or space.

INVESTOR'S SNAPSHOTS

EXPLANATORY NOTES

SALES in the Investor's Snapshots elsewhere in the magazine exclude excise taxes. Instead of sales, assets are shown for commercial banking companies, diversified financial companies, life insurance companies, and utilities, and operating revenues for transportation companies.

NET PROFIT includes any extraordinary items. Where applicable, sales and net profit for past quarters are restated to reflect mergers, acquisitions, or divestitures.

RETURN ON COMMON STOCKHOLDERS' EQUITY is calculated for the latest four quarters after subtracting dividends paid on preferred stock from net income. The five-year average is based on the last five full fiscal years.

PRICE/EARNINGS MULTIPLE is based on earnings per share for the latest four quarters.

TOTAL RETURN TO INVESTORS includes stock price changes and assumes dividends are reinvested on the date paid.